

MONTGOMERY COUNTY MARYLAND

Comprehensive Annual Financial Report



Fiscal Year 2004

**July 1, 2003 - June 30, 2004
Rockville, Maryland**

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Montgomery County,
Maryland

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2003

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



A handwritten signature in black ink, reading "Edward Hanafin".

President

A handwritten signature in black ink, reading "Jeffrey R. Enen".

Executive Director

MONTGOMERY COUNTY MARYLAND

Comprehensive Annual Financial Report



Prepared by the
DEPARTMENT OF FINANCE

Timothy L. Firestine, Director
101 Monroe Street
Rockville, Maryland 20850
240-777-8860

Fiscal Year 2004
July 1, 2003 - June 30, 2004





Montgomery County

Vision Statement

*“Helping to make Montgomery County
the best place to be through efficient, effective and
responsive government that delivers quality services.”*

Guiding Principles

We Will Provide Excellence in Government By:

- Insisting upon customer satisfaction
- Ensuring high value for tax dollars
- Adhering to the highest ethical standards
- Appreciating diversity
- Being open, accessible and responsive
- Empowering and supporting employees
- Striving for continuous improvement
- Working together as a team
- Being accountable

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INTRODUCTORY SECTION



DEPARTMENT OF FINANCE

Douglas M. Duncan
County Executive

December 3, 2004

Timothy L. Firestine
Director

Honorable County Executive,
Members of the Montgomery County Council, and
Chief Administrative Officer

Ladies and Gentlemen:

I am pleased to present the Comprehensive Annual Financial Report (CAFR) of Montgomery County, Maryland (the County), for the fiscal year ended June 30, 2004. This report, presented in conformity with accounting principles generally accepted in the United States of America (GAAP), was prepared by the County's Department of Finance in cooperation with the finance departments of the County's component unit and joint venture organizations.

This report has been prepared pursuant to the provisions of Article 2, Section 214 of the Charter of the County, and includes the independent auditors' opinion, issued by the County Council appointed independent public accounting firm, as provided by Article 3, Section 315 of the County Charter. The County is responsible for the completeness and fairness of the information, including disclosures, presented in this report. We believe the information presented in this report is complete and accurate in all material respects, and that it fairly presents the County's financial position and results of operations.

To provide a reasonable basis for making these representations, management of the County has established a comprehensive internal control framework. Because the cost of internal controls should not exceed the anticipated benefits, the objective is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatement.

The public accounting firm of KPMG LLP has performed an independent audit of, and issued an unqualified opinion on, the County's financial statements as of and for the year ended June 30, 2004. The independent auditors' report is located at the front of the financial section of this report. This independent audit of the County's financial statements was part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The independent auditors' reports associated with this audit are available in the County's separately issued Report on Expenditures of Federal Awards.

Overview of the Report

The accompanying report consists of four sections: introductory, financial, statistical, and index.

The introductory section includes this transmittal letter, a copy of our Certificate of Achievement for Excellence in Financial Reporting awarded for the FY03 report, a list of special acknowledgments, the Montgomery County, Maryland organization chart, and a listing of officials.

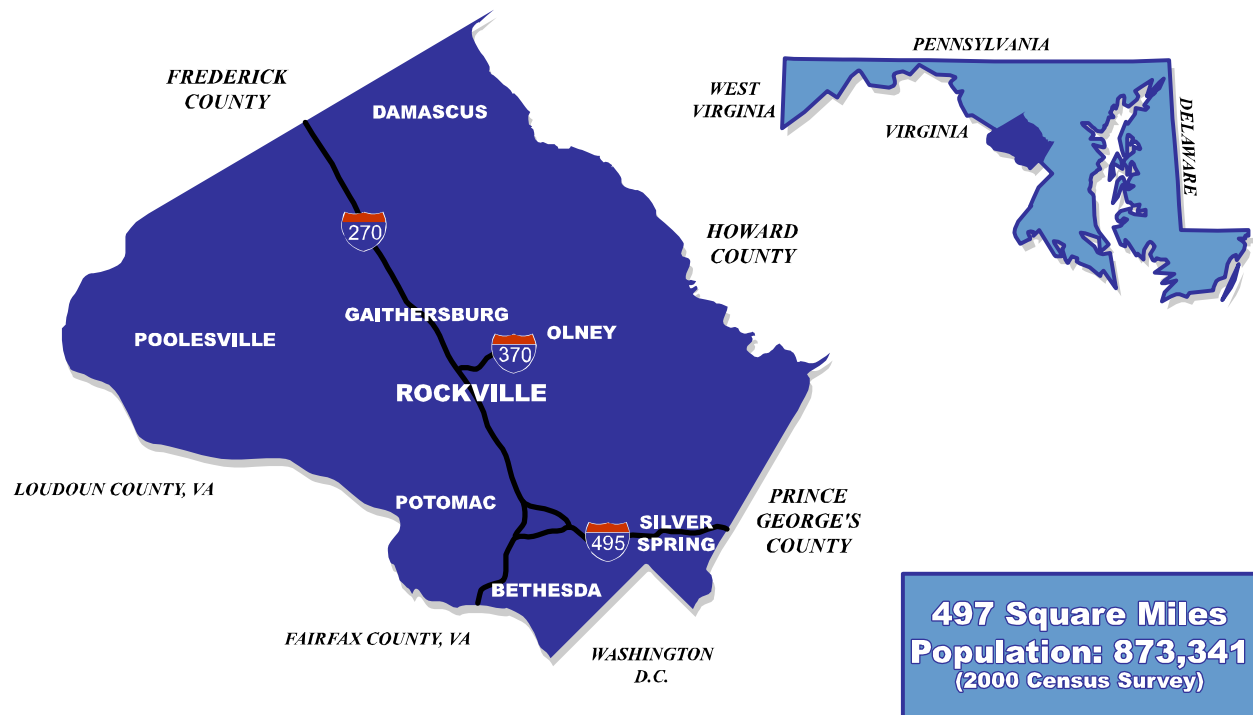
The financial section includes the report of the independent auditors, MD&A, the basic financial statements, and the combining and individual fund financial statements and supplementary schedules. GAAP require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of MD&A. This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The MD&A can be found immediately following the report of the independent auditors.

The statistical section includes selected information on financial trends, revenue capacity, debt capacity, demographic and economic data, and operating data, financial and demographic information, generally presented on a multi-year basis. The statistical section incorporates, earlier than required, certain new information mandated by Governmental Accounting Standards Board (GASB) Statement No. 44, *Economic Condition Reporting: The Statistical Section*. The County anticipates implementing the remaining information prior to or as of FY06, which is the official effective date of this Standard.

The index is presented solely to facilitate the identification of financial statements of the individual funds and component units of the County.

PROFILE OF THE GOVERNMENT

Montgomery County, named after the early American general, Richard Montgomery, was established in 1776 by the State Convention. The County government was structured under the County Commission system until 1948, when voters adopted a charter, which gave the County home rule and a council-manager form of government. The governing authority of the County, today, is still the charter, which was fully implemented in 1970, with the election of an executive and a council. Currently, Montgomery County is the most populated and affluent jurisdiction in Maryland and enjoys the distinction of being named an All-American community.



Budgetary Overview

The annual budget provides the basis for coordinating and controlling the County government programs and expenditures, which include education, public safety, public works and transportation, culture and recreation, health and human services, community development and housing, environment, and general government services. The County Executive develops and recommends budget proposals and the County Council then authorizes expenditures and sets property tax rates. Expenditure authority is provided at the fund and department level in three major categories (personnel costs, operating and capital outlay). The County Executive has authority to transfer appropriations within departments up to 10 percent of the original appropriation. Transfers between departments are also limited to 10 percent of original appropriation and require County Council action. Additional spending

authority, in the form of supplemental or special appropriations, may also be approved by the County Council during the year.

A budget-to-actual comparison statement for the General Fund is presented on Exhibit A-7 as part of the basic financial statements. Budget-to-actual comparison schedules for other funds with legally adopted budgets are presented in the Supplementary Data section.

The Reporting Entity

The following organizations are included as component units in the accompanying financial statements: Montgomery County Public Schools (MCPS), Montgomery Community College (MCC), Housing Opportunities Commission of Montgomery County (HOC), Montgomery County Revenue Authority (MCRA), and Bethesda Urban Partnership, Inc. (BUPI).

The County's participation in the following joint ventures is also disclosed in the Notes to the Financial Statements (see Note IV-D): Maryland-National Capital Park and Planning Commission, Washington Suburban Sanitary Commission, Washington Suburban Transit Commission, Washington Metropolitan Area Transit Authority, Metropolitan Washington Council of Governments, and Northeast Maryland Waste Disposal Authority.

Copies of the respective independently audited annual financial reports required by State or County law are available from the above mentioned component units and joint ventures.

INFORMATION ON ECONOMIC CONDITION

The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the specific environment within which Montgomery County operates.

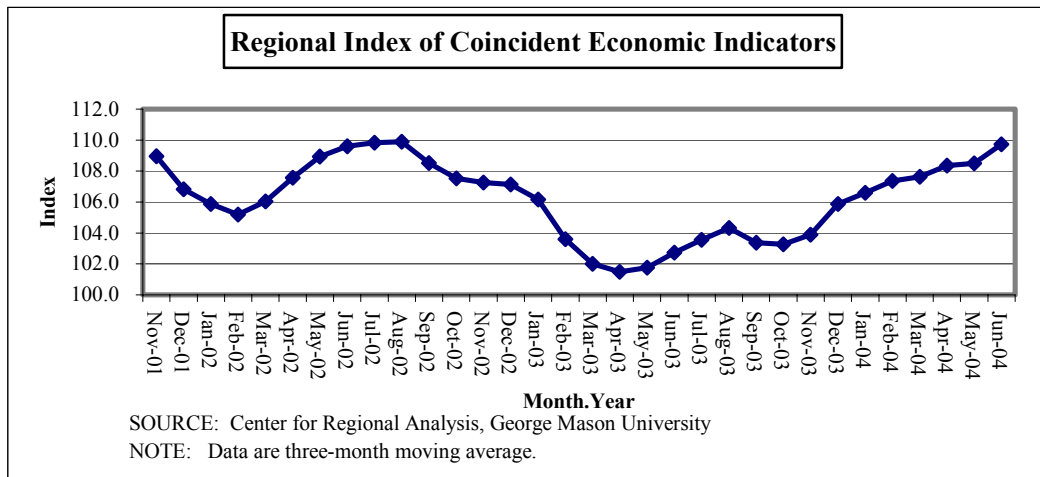
Overview of National Economic Condition and Outlook

As FY04 began, the nation's economy was expanding at an annual rate of 4.1 percent with real gross domestic product at \$10.3 trillion, payroll employment stood at 129.9 million, the unemployment rate was 6.3 percent, and the "core" inflation was 1.5 percent. Interest rates were at their historic lows with rates on 30-year fixed rate mortgages at 5.24 percent and the effective rate on federal funds at 1.08 percent, which followed a rate cut of 25 basis points by the Federal Reserve's Federal Open Market Committee (FOMC) on June 25, 2003. At the end of FY04, the nation's economy grew an additional 4.4 percent with real gross domestic product at \$10.8 trillion, "core" inflation increased only 1.9 percent, mortgage rates increased to 6.25 percent, and the effective rate on federal funds was up to 1.38 percent, which included a rate hike of 25 basis points on June 30, 2004. Because of the economic expansion during FY04, the economy added 1.4 million jobs, an increase of 1.1 percent, and the unemployment rate dropped to 5.6 percent by June 2004. Most of the gain, or nearly 65 percent, in employment occurred during the months of March through May with the addition of 900,000 jobs. However, while most economic indicators suggested a marked economic improvement during FY04, oil prices reached historic highs by the end of FY04. At the beginning of FY04, the spot price of West Texas Intermediate Crude was \$31 per barrel. By the end of FY04, the spot price stood at \$40 per barrel, or a 29 percent increase. At that time, the spot price in June 2004 was the highest price ever.

The Local Economy

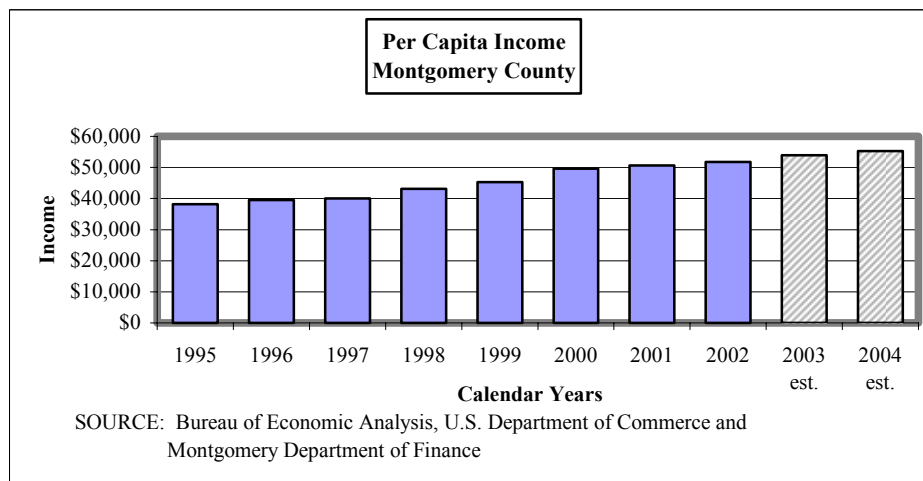
Because the region's economy is significantly dependent on spending by the federal government, the recent surge in federal procurement boosted the region's economy during FY04. According to data from the Center for Regional Analysis, George Mason University, the Washington Coincident Index, which represents the current state of the region's economy, increased 6.8 percent in FY04 compared to the 2.7 percent for the National Coincident Index. Since the beginning of the fiscal year, the region's economy added 79,000 new jobs, the largest increase among the major metropolitan areas, and the unemployment rate has held steady at 3.3 percent, one of the lowest among the largest metropolitan areas in the country. The recent surge in the local economy is also reflected in the performance of local businesses. Over the past two years, the Washington Post-Bloomberg regional index

increased almost 62 percent compared to the 53 percent increase in the broad-based Russell 2000 index. Retail sales were up 8.2 percent for the year compared to 5.0 in FY03.



Personal Income

On a calendar year (CY) basis, per capita income increased from approximately \$38,000 in CY95 to an estimated \$55,300 in CY04 – an annual average rate of 4.1 percent. However, over the past ten years, the rate of growth in per capita income experienced three distinct cycles. Between years CY94 through CY97, income grew at a 2.7 percent annual rate, and between years CY97 and CY02, it grew at a 7.2 percent annual rate. However, given the modest growth of new jobs in CY03 and the first quarter of CY04, the acceleration in the growth in per capita income experienced during the CY97 through CY02 period is not sustainable and as such it is expected to grow at an average annual rate of 1.7 percent from CY02 through CY04.



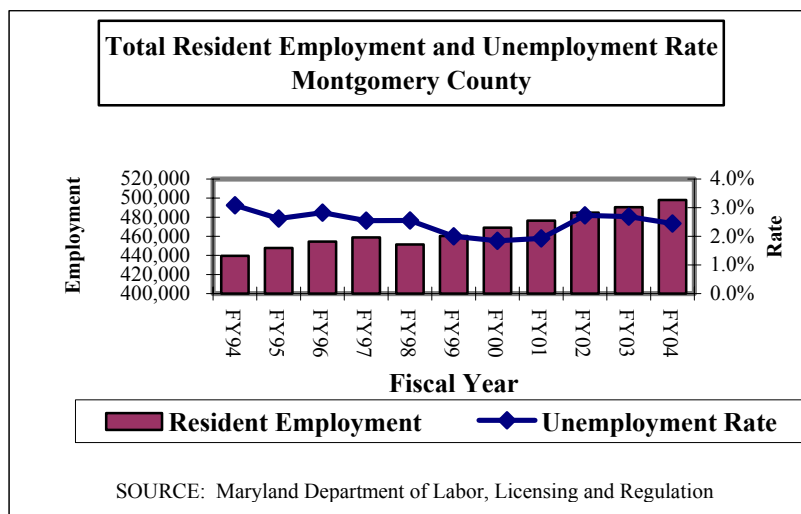
Employment

As FY04 began, the labor force in Montgomery County stood at 509,935, employment for County residents was 495,254, and the unemployment rate was 2.9 percent. By the end of the fiscal year, the labor force increased by 8,959, or 1.8 percent, the largest increase in two years. Employment for County residents increased slightly greater than the labor force at 10,973 or 2.2 percent, thereby resulting in a lower unemployment rate of 2.4 percent by the end of the fiscal year. However, total payroll employment during CY03, the latest date for which data are available, presented a much different picture of the employment situation in Montgomery County. During

CY03, the number of payroll jobs in the County increased nearly 1,800, or 0.4 percent, but slightly less compared to CY02 (an increase of 2,250 jobs or 0.5 percent). Payroll employment is a better indicator of the economic activity and employment situation in Montgomery County than employment by place of residence for it provides a measure of the strength of the County's economy.

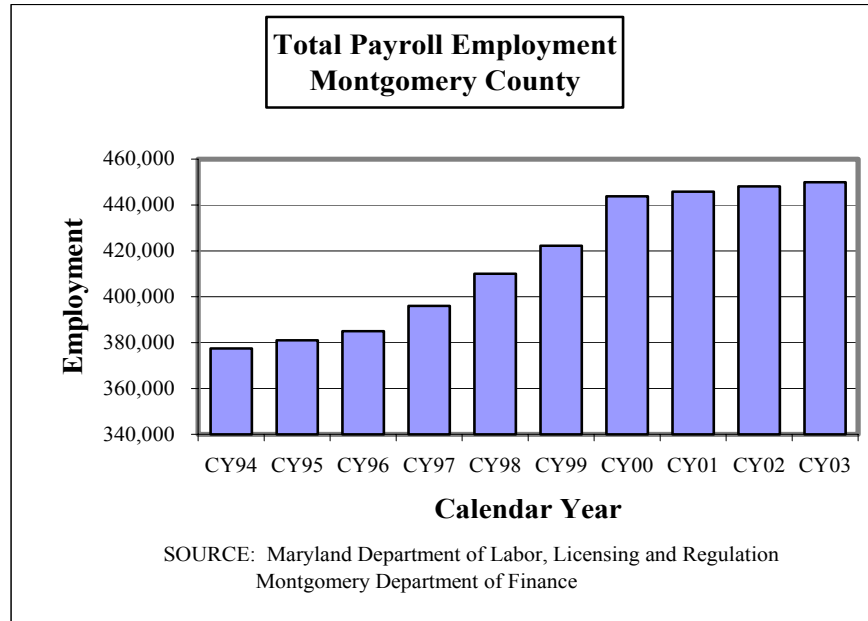
Labor Force and Resident Employment

The average total labor force in Montgomery County stood at 510,509 in FY04, which was slightly higher than the 509,935 when the fiscal year began and an increase of 1.3 percent over the average for FY03. Average resident employment also increased during FY04 to 498,022 compared to the average of 490,509 for FY02 – an increase of 1.5 percent. Unlike total payroll employment, resident employment experienced modest growth in FY04 when compared to the ten-year average of 1.3 percent. Such an increase in resident employment exceeded the growth in the labor force, thereby contributing to the decline in the unemployment rate from an average of 2.7 percent in FY03 to 2.4 percent in FY04.



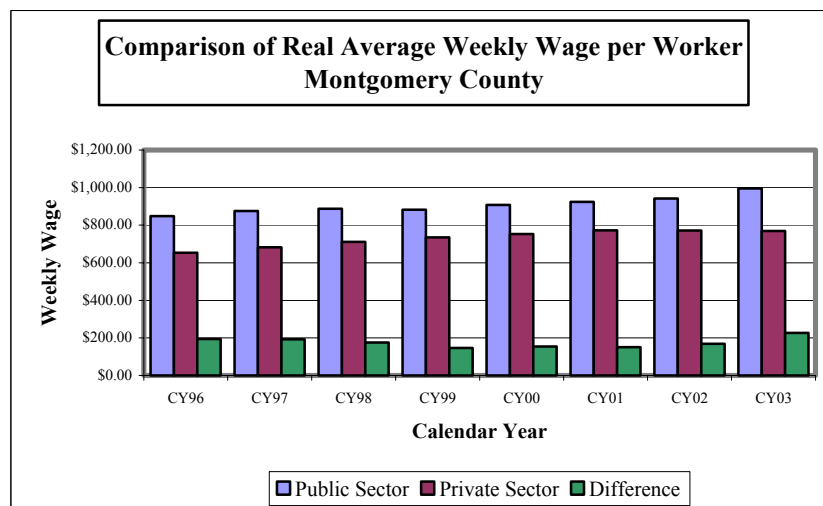
Payroll Employment

Because Montgomery County is a suburb of Washington, D.C., thirty-percent of the County's economy is attributed to the presence of the federal government. Such importance is reflected in payroll employment in the proportion of total jobs held by federal employees. Over the past two years, the number of federal government jobs increased by slightly less than 950, while the private-sector added less than 1,200 jobs. The proportion of employees in the federal government compared to total payroll employment has held steady at approximately 9 percent over the past five years, down from the 11 percent average during the CY93-CY99 period. While employment in the private-sector industries increased in CY03, the financial services sector experienced the most significant increase in jobs followed by the professional and business services, education and health services, and leisure and hospitality sectors. Because of the concentration of employment in the service-providing sectors of the economy, Montgomery County has not been as susceptible to major contractions in private-sector employment, particularly within the goods-producing sector, during this economic expansion period. Nevertheless, during CY03, the County lost 1,000 manufacturing and 1,200 information technology jobs compared to the same period in CY02.



Payroll Wages and Salaries

Total payroll wages in the County were \$22.0 billion in CY03, the latest period for which data are available. This amount represents a 2.8 percent increase over CY02 in nominal dollars but did not increase in real dollars, i.e., adjusted for inflation. While total payroll wages increased in nominal terms during CY03, there was a difference between wages received by public-sector versus private-sector employees. Total wages of public-sector employees increased 3.0 percent during CY03 or 0.2 percent in real terms. Federal government employees were the largest beneficiary within the public sector with wages increasing 7.5 percent or 4.6 percent in real terms. Based on average weekly wages, federal employees received almost \$1,450 in compensation which was 67 percent above compensation received by local government and private-sector employees.



The increase in total nominal wages in the private-sector was only 2.7 percent over CY02, but a decline of 0.1 percent in real terms, and average weekly wages per private-sector worker increased only 2.4 percent in CY03, which presents a decline of 0.4 percent in real terms. Those changes in private-sector wages suggest that employers

in Montgomery County, excluding the public sector, appear to be reluctant to hire and to increase wages and salaries above the rate of inflation.

Because of the importance of the federal government in the County's economy, particularly in payroll employment, and the reluctance of private companies to hire and to increase wages and salaries, the disparity between the public and private sector wages has steadily increased over the past two years. Expressed in real wages, the difference in weekly average salaries increased from \$147 in CY99 to \$226 in CY03.

Real Estate

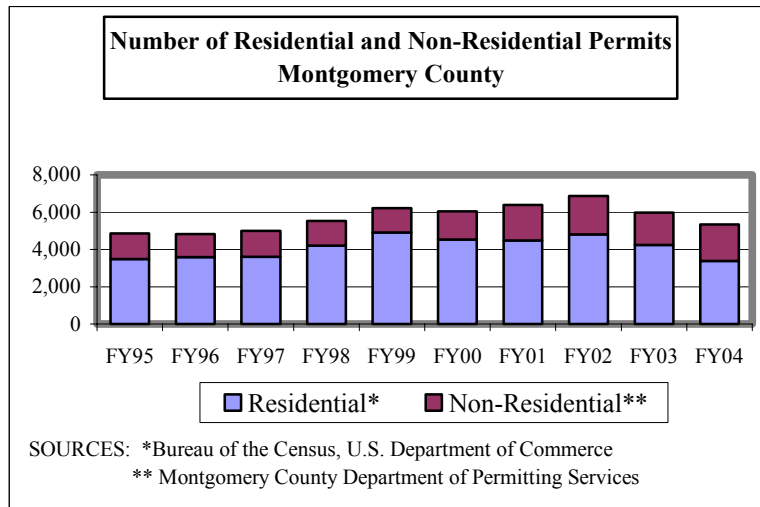
Construction and real estate activity play a significant role in Montgomery County's economy. First, nearly 40 percent of the County's General Fund revenues are derived from the property tax base. Second, the construction industry was the only goods-producing sector that added over 200 jobs in CY03. Nonresidential-residential construction activity tends to be very volatile from one year to the next, while residential construction exhibits a more medium-term cycle. Such volatile and cyclical trends have had significant effects on the County's economy.

Permits

Permit authorizations are an indicator of planned construction activity in nonresidential-residential and residential real estate sectors and are granted by Montgomery County's Department of Permitting Services (DPS). The total number of nonresidential-residential and residential permits for the County for the past ten fiscal years is presented in the graph below and suggests that the cycle for total permits is of a three- to four-year duration with volatile, yet offsetting, annual changes between nonresidential-residential and residential permits. The total number of permits authorized in FY04 was 5,334, a decrease of 10.7 percent and the second consecutive annual decrease. The two-year drop in total permits is solely attributed to the decline in residential permits, while the number of nonresidential-residential permits issued in FY04 increased nearly 13 percent. Since the number of residential permits issued by DPS exceeds nonresidential-residential permits by an average ratio 1.6:1, a significant decline in residential permits will affect the change in total permits.

The increase in nonresidential-residential permits followed a decline in FY03. However, over the prior three-year period (FY00-FY02), the number of nonresidential-residential permits issued by DPS increased 57.5 percent suggesting a potential construction boom that continued into FY04 with a slight pause during FY03. In fact, the number of nonresidential-residential permits issued in FY04 (1,946) was the second largest during the past ten years with the largest issuance occurring in FY02 (2,059).

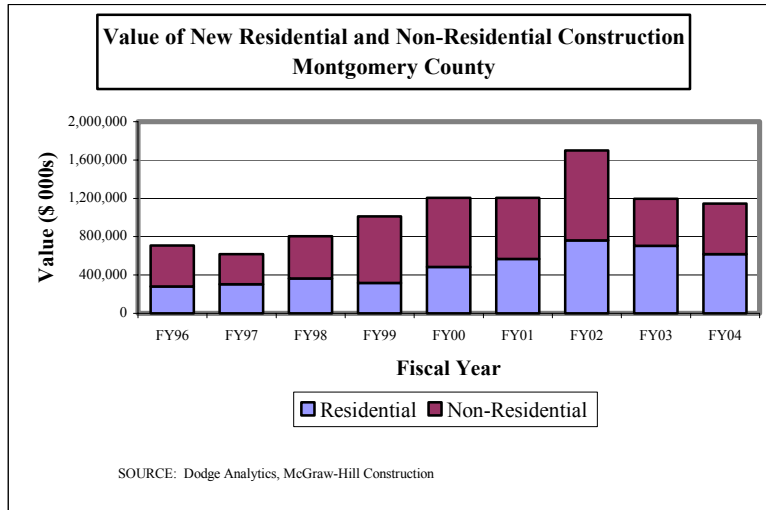
However, the residential sector experienced a rapid decline during the past five years (FY00-FY04). Over that period, the number of residential permits issued declined during four of those years with a modest increase in FY02. Since reaching a peak of 4,915 permits in FY99, the number of residential permits issued by DPS has steadily declined, save FY02, indicating that the level of residential construction has dropped dramatically in the County and below the capacity required to provide for replacement of existing housing stock and formation of new households. While the percentage of residential permits to total permits issued remained above its 70 percent level between FY95 and FY03, it dropped below that level in FY04 (63.5 percent).



Construction Starts

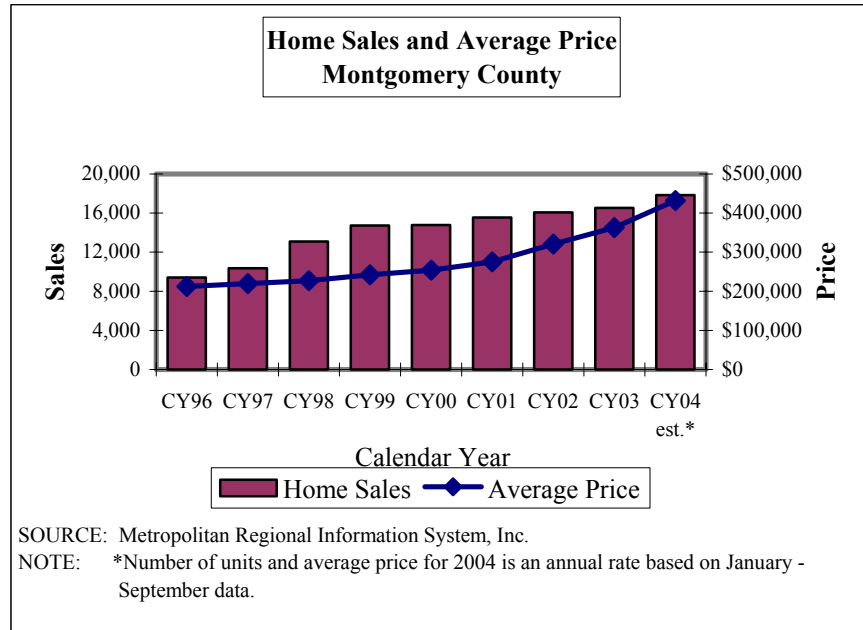
Along with permit authorizations, construction starts measure the potential level of the supply of real estate property in the near term. The number of construction projects or starts in the County for nonresidential-residential and residential properties was 2,768 in FY04 – a decrease of almost 1,300 construction starts or 31.9 percent from FY03. As the graph below illustrates, that decline was the second year in a row and followed four years of growth in total construction in Montgomery County. Such a drop over two consecutive years suggests that construction activity has reached a pause after double-digit growth that occurred during the FY99-FY01 period. Unlike the issuance of permits, both nonresidential-residential and residential construction starts declined in FY04, the second consecutive year in which both sectors declined during the same fiscal year. Since both permit authorizations and construction starts declined sharply in FY04, such decreases suggest that the boom experienced in prior years, particularly in the nonresidential-residential sector, has halted. The value of total construction declined to \$1.1 billion in FY04 or 4.0 percent, which was solely attributed to the decline in the value of residential construction. That decline was the second consecutive annual decline after achieving a record high of \$1.7 billion in FY02. While the number of construction projects declined in FY04, the value of construction put in place experienced less of a decline as measured by historical standards. For purposes of property tax revenues, it is the value of new construction rather than the number of projects that is relevant in determining the amount of additional property added to the County's assessable base.

Because of the close association between the issuance of permits and the start of construction, one would expect that the construction cycle for both nonresidential-residential and residential starts would follow a similar pattern as the permitting cycle. While such an association was evident during FY03 and FY04, this is not always the case, as there is a long lead time between authorization and construction. While one would expect a long lead time between authorization and construction to exist in nonresidential-residential construction, such a lead time with residential property is much shorter. There is an average of four months from the issuance of a residential permit to the start of construction for residential projects. Therefore, the trend between the number of permits issued and the number of construction starts is almost contemporaneous. The number of residential permits authorized in FY04 declined 20.2 percent while the number of construction starts declined 33.7 percent. The value of new residential construction also declined 12.3 percent in FY04 to a \$619.0 million. While the percentage decline appears dramatic, the value of new residential construction was the third highest during the last eight years and was only exceeded by the previous two year's of \$762.6 million in FY02 and \$705.8 million in FY03. Such a phenomenon suggests developers are building larger and more expensive homes in the County during the past three years.



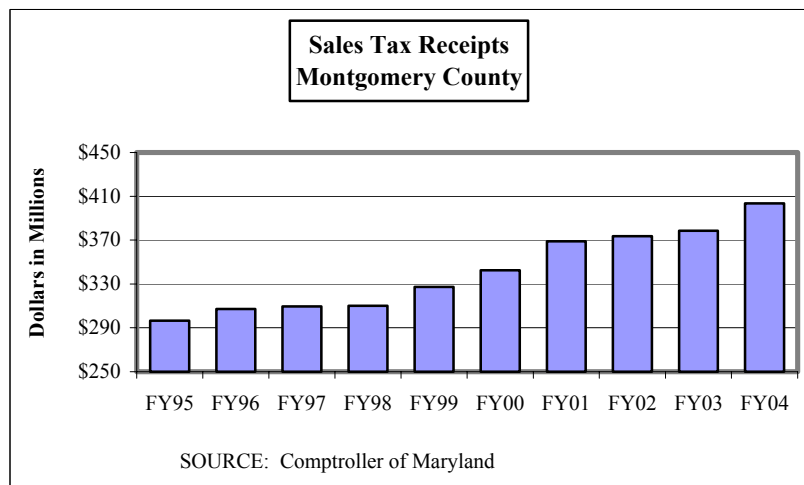
Home Sales

With the decrease in the number of residential construction projects during the past two years and the current level of 30-year fixed mortgage interest rates at historic lows, one would expect dramatic growth of home prices in the County. As the accompanying graph illustrates, home sales in CY04 are expected to increase 7.9 percent, which is above the recent three-year average (CY01-CY03) of 3.8 percent and a significant rebound from last year's 2.9 percent, which was one of the lowest increases in seven years. While home sales are expected to rebound this calendar year, average prices have continued their significant acceleration during CY04 outpacing the percentage increase in sales. Prior to CY02, the sales of existing homes averaged almost 11 percent per year, while the average annual increase in home prices was only 5.4 percent. Because of the dramatic decline in the stock market between CY00 and CY02 and the significant decline in mortgage rates, some individuals appear to have shifted their investment in corporate equities and mutual funds to real estate. Together with a continued growth in the formation of new households, it created a significant demand for housing in the County such that average home prices increased 16.6 percent in CY02, 13.2 percent in CY03, and an estimated 19 percent in CY04, while percentage sales were much higher. Therefore the dramatic increase in home prices in the County may be attributed to three factors: an insufficient supply of new homes due to a limited availability of suitable land for development, an investment portfolio shift by individuals and households from corporate equities and mutual funds to real estate because of the lackluster performance in the stock market, and low mortgage interest rates. The significant increase in home prices over the past three years also has had an effect on reassessments in the County. In FY99, total reassessments for residential property including homes, apartments, and condominiums were \$653.9 million and by FY04 reached \$6,273.4 million – a nearly tenfold increase. That rate of increase was the highest since the early 1990s.



Retail Sales

Retail sales are the most closely watched indicator for judging the strength of consumer confidence and demand. Sales tax receipts provide an indication of the strength of consumer spending in Montgomery County. Sales tax receipts are divided into nondurable and durable goods. The sale of nondurable goods is an indicator of consumer confidence about the current economic condition in the County while the sale of durable goods is an indicator of consumer's expectations about future economic activity. Sales tax receipts experienced four distinct cycles over the past ten fiscal years, a period (FY95-FY96) of 9.3 percent growth in tax receipts, a period (FY97-FY98) of 1.0 percent growth, a period (FY99-FY01) of 18.9 percent growth, and finally a period of 2.6 percent growth (FY02-FY03). Sales tax receipts stood at \$403.6 million in FY04, an increase of 6.6 percent and the largest increase since FY01 (7.6 percent). Sales of nondurable goods grew 5.9 percent while sales of durable goods were up 8.3 percent.



Consumer Prices

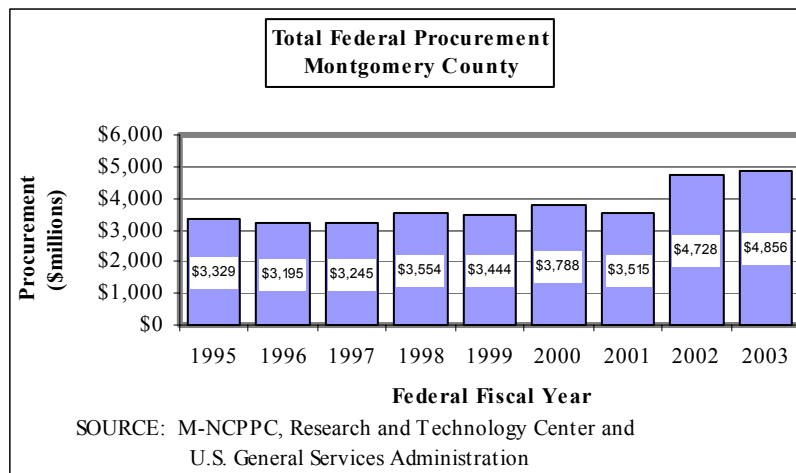
The consumer price index for all items excluding food and energy for the Washington-Baltimore Consolidated Metropolitan Statistical Area (CMSA) increased 1.7 percent in FY04 which was lower than in FY03 (2.7 percent) but higher than the nation (1.4 percent). Since the U.S. Bureau of Labor Statistics began reporting the index for the region, the increases in the regional core consumer price index exceeded the national rate the past three fiscal years by 1.5 percentage points largely attributed to increases in the cost of housing and medical care.

Federal Procurement Spending

According to data provided by the Planning Department of the Maryland-National Capital Park and Planning Commission and the U.S. General Services Administration (GSA), businesses in Montgomery County received \$4.9 billion in procurement contracts from the federal government for federal fiscal year (FFY) 2003 (October 1, 2002 through September 30, 2003). This represents an increase of 2.7 percent over the previous FFY and is the highest in the County's history. Between FFY95 and FFY02, federal procurement averaged approximately \$3.4 billion per year, and in FFY03 it reached \$4.7 billion.

The increase in procurement during FFY03 reflects a shift in government funding to domestic programs compared to FFY02. In FFY02, the dramatic increase in procurement was attributed to the federal government's immediate response to geopolitical events such as the 9/11 terrorist attack and a significant increase in defense spending. In FFY03, procurements from the Department of Defense were \$1.2 billion, a decrease from \$1.3 billion in the previous year. In contrast, procurement from the National Institutes of Health (NIH), which represents the largest federal agency in the County, and the Departments of Education and Energy increased to \$1.2 billion, \$213.6 million, and \$146.6 million, respectively.

While the procurement dollars increased in FFY03, the effect of federal largess in the County's economy did not provide complete immunization from a sluggish economy. Such growth did not immediately increase payroll employment in some sectors.

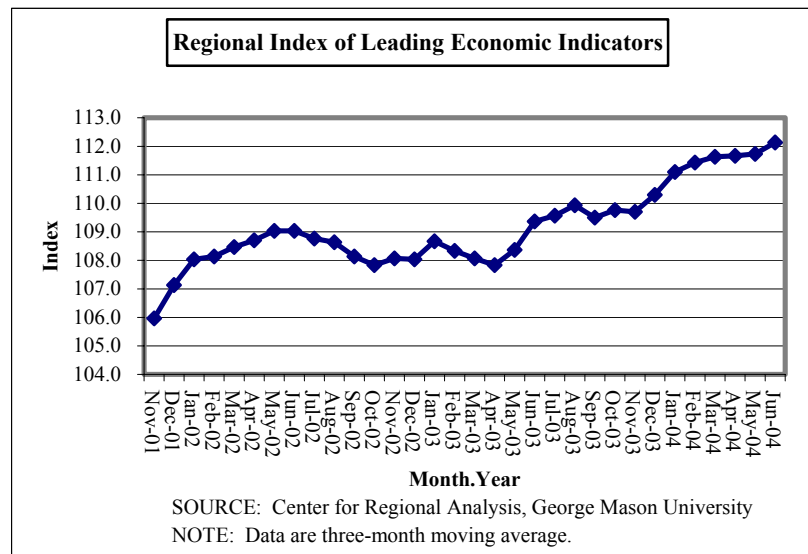


Future Economic Outlook

Following a year whereby the County's economy experienced modest growth in employment, a rebound in consumer spending, but a decline in both residential and nonresidential construction, the outlook for FY05 is expected to see modest increases in employment, consumer spending, and nonresidential-residential construction, but continued sluggish activity in residential construction. With mortgage rates remaining at historic low levels, home sales are expected to increase through the remainder of CY04 and home prices to increase at double-digit rates. However, the real estate market remains uncertain for CY05. Private-sector payroll employment is expected to improve due to another round of increases in federal procurement.

At the national level, the Federal Reserve is expected to continue to raise the target in interest rate for federal funds. Based on data from the Chicago Board of Trade, the rate is expected to reach 2.5 percent by the end of FY05. Interest rates on 30-year fixed rate mortgages are expected to remain below 6 percent through the rest of CY04, but the housing industry expects rates to climb to the 6.5-7.0 percent range by the end of CY05. The effect such increases will have on the housing market is that sales are expected to decline by an average of 11 percent in CY05. The weak performance of the stock market during the first half of CY04 has had a negative effect on both business and consumer confidence. While the volatility in the stock market has been the result of both psychological and economic factors, it is a measure for assessing future corporate earnings. Since the economic recession ended in November 2001 and the stock market began its recovery in March 2003, business profits have improved, but companies have been reluctant to hire new workers. Most of their efforts to improve corporate earnings have been in reducing excess capacity and increasing worker productivity. With the growth rate of the population increasing one percent per year, real gross domestic product (GDP) must increase nearly four percent per year before employment increases and the current unemployment rate decreases. Given that the real GDP growth rate in FY04 was 4.4 percent, double the 2.2 percent in FY03, the economy added 1.4 million jobs, while it lost almost half a million jobs during FY03. Based on the August 2004 survey of 30 forecasters, the Federal Reserve Bank of Philadelphia estimates a real GDP growth rate of 3.8 percent in FY05. Such a rate is needed for significant growth in payroll employment. The survey estimates 1.8 percent growth in jobs, or 2.4 million, in CY05.

Since June 2003, the regional index of leading indicators developed by CRA for the Washington metropolitan area suggested a scenario of improved economic activity during FY04. Over the past six months, the index increased 1.6 percent suggesting that the regional economy will continue to expand into FY05 but at a much slower rate compared to FY04.



The assumptions underlying an improvement in the County's economy during FY05 are the continuation of low interest rates especially home mortgage rates, a decline in the "core" inflation rate, consistent consumer confidence, and a rebound in payroll employment largely attributed to the increase in federal procurement.

MAJOR INITIATIVES

Major initiatives of the County during FY04, including certain initiatives of its component units, presented by functional area, include the following:

Community Development and Housing

Low-Income and Elderly Housing: As part of the continuing implementation of the County's Housing Policy, Montgomery County-A Place To Call Home, the Department of Housing and Community Affairs, in conjunction with a national nonprofit-profit housing developer, Homes for America, preserved Charter House, a 212-unit high-rise apartment building for the elderly in Silver Spring. In addition, County funds have assisted in the financing of two new developments for low-income seniors-Olney Manor (102 units) and Randolph Manor (83 units). County funds were also used to finance the purchase and rehabilitation of a 187-unit federally assisted senior rental property in the City of Takoma Park-Takoma Towers.

Montgomery County Conference Center: The Montgomery County Conference Center neared completion in FY04. The facility will consist of a 100,000 square foot conference center next to a full-service 225 room Marriott Hotel. Within the center will be 13,000 square feet of meeting rooms, a 130-seat amphitheater, and 20,000 square feet of public open space. When it opens in November 2004, it will contain the third largest ballroom in the Washington, D.C. metropolitan area.

Wheaton Redevelopment: Substantial progress is being achieved in transforming Wheaton into a vibrant downtown center with a balanced mix of residential, office, and retail uses typical of an urban environment. Development activity has been initiated by the private sector on seven key gateway sites that at completion will create nearly 2 million square feet of new development and generate over \$280 million in private capital investment. These developments will create 744 residential units, nearly 600,000 square feet of new retail and 300,000-400,000 square feet of new office space in the downtown area. Westfield Corporation, owners of Westfield Shoppingtown Wheaton, has secured Macy's as its fourth anchor store, and is adding a second level with another 100,000 square feet and 50 new specialty stores to its existing 850,000 square foot mall.

Silver Spring Redevelopment: The \$165 million redevelopment of downtown Silver Spring continued to move forward in 2004. A number of new stores, restaurants, and other amenities opened their doors, including a 20-screen movie theater with stadium seating. The County also neared completion of the 19,000 square foot Silver Spring Innovation Center, an information technology incubator in downtown Silver Spring. The facility is the County's second business incubator and is scheduled to officially open in September 2004. The facility is designed to accommodate 25 to 35 early stage companies every three year cycle.

Marketing & Business Development: The Department of Economic Development staff assisted 19 companies in expanding in or relocating to Montgomery County in 2004, retaining or adding over 1,600 jobs in the County. These projects resulted in nearly 500,000 square feet of newly occupied space and almost \$100 million in capital investment.

Culture and Recreation

Libraries: The renovation of the Bethesda Library was completed, with the library reopening for service in October 2003. This \$3.2 million project provided an improved area for children's services, improved space for library collections and technology, as well as updating all mechanical equipment and energy efficiency. Ground was broken for the new Germantown Library in April 2004. This 44,000 square foot building in the new Germantown Town Center will replace the existing 16,000 square foot Germantown Library located in the Upcounty Services Center. The new library will have a collection of 200,000 volumes to serve the growing Germantown community. The total project cost is \$19.2 million.

Facility Development: The Martin Luther King Outdoor Pool was opened, which includes a leisure pool with the County's first "Lazy River" tube float experience, three major water slides, a fitness/competition pool, and numerous spray and soaking elements. The County also opened its first "Spray Park" at the Good Hope Neighborhood Center.

Education

Higher Education:

- The Takoma Park Campus of Montgomery College (MCC) is undergoing an \$88 million expansion that will extend the campus into the heart of south Silver Spring along the Georgia Avenue corridor. The project marks the single largest capital venture for the College since the creation of the Germantown Campus in the 1970's, and is widely seen as a vital component of the revitalization of downtown Silver Spring. The expansion will proceed in three phases over the next six years. Construction on Phase I, the 98,000 square foot Health Sciences Center, began in the fall of 2002 and was completed in 2004. Phase II, the Student Life Center and Pedestrian Bridge, began construction in 2004, with an anticipated completion date of 2006. Phase III, the Cultural Arts Center, will begin construction in 2006, with completion expected by 2008.
- In early 2003, MCC settled on the purchase of a 20-acre site adjacent to College's Germantown campus. This property was combined with 20-acres of existing undeveloped land on the campus to form a 40-acre site on which a 1 million square foot science and technology center will be constructed. The preliminary plan for the science and technology center calls primarily for high technology research and development space, with a focus on the life sciences, which will complement the biotechnology programs and curriculum already offered at the Germantown campus. As part of the County's investment in the purchase of the land, the County will be granted a 5-acre site on the property to construct and manage a high technology incubator for start-up companies. The County has begun initial work on the design, location, and implementation of this incubator facility.

Secondary Education: MCPS continues to experience enrollment growth. MCPS enrollment was 139,203 students in FY04, 312 more than in FY03. The September 30, 2004, enrollment is projected to be 140,492. To relieve overcrowding, accommodate more full-day kindergarten classes, and provide for increased enrollment, MCPS added 52 classrooms to six schools in FY04, reopened a high school and will add another 43 classrooms to six schools in FY06.

The 2004 graduating class achieved the highest ever SAT scores. The systemwide average SAT score was 1,102, an eight point improvement compared with 2003. The average included the highest ever mathematics score (561) and the highest average verbal score in 12 years (541). The higher SAT scores mark the achievements of the first graduating class taking the SAT who were exposed to the full range of ongoing high school reforms in MCPS.

Environment (Including Solid Waste Activities)

Regional Wind Energy Purchase: The Department of Environmental Protection led a wind energy purchase by a regional partnership, whereby, beginning July 2004, five percent of the electricity used by this partnership comes from wind energy. This amount (over 38.4 million kilowatt hours per year) represents the largest wind purchase ever conducted by a local government organization in the United States. A unique feature of this purchase is its inclusion in the regional implementation plan (Metropolitan Washington Regional SIP) for meeting ground-level ozone standards under the Clean Air Act.

Recycling Center: Generating over \$2.2 million in total net revenue in FY04, the Recycling Center realized the highest revenue since the facility began operations in 1991. FY04 was the first full year of operations using the new processing system, which afforded the ability to sort more types of plastic, realizing greater revenue, and the ability to produce purer products. These factors increased competition among vendors bidding for the county's recyclable products. The advantages of the new processing system, including increased revenue, were instrumental in the facility's competing and receiving the Solid Waste Association of North America's (SWANA) 2004 gold medal for recycling excellence.

RRF Contract Re-negotiation Savings: The County renegotiated its contract with the Resource Recovery Facility (RRF) in FY04 for FY05, which will result in savings (based on budget tonnages and other budget assumptions) of \$3.5 million. Annual savings in future years, through the end of the contract period (2013), will be similar for similar tonnages or slightly less in years experiencing lesser tonnages.

General Government

Finance Web-based Tax Lien Sale Process: The Department of Finance (Finance) developed the “Service Oriented–Intelligent Bidders’ Web Tool,” a simplified web-based government-to-business auction process, which sells tax liens for unpaid property taxes to the public. This system ensures that (a) all tax liens are sold, (b) the County collects all delinquent property taxes and related penalty and interest charges, (c) the process takes a minimum amount of time, and (d) considerable time and money is saved by the County, taxpayer, and investor. At the same time, the integrity of the public auction process is ensured. Distinctive features include: daily updates of delinquent properties and the group to which they are assigned; a high bid premium calculator; a download capability; and the Submit Bid feature which is only available on the bidding date and designated time period to ensure system integrity during the submission of the sealed bid.

Electronic Timesheet Management and Reporting System: Finance began a multi-year project to replace the County’s current paper timesheet process with a web-based electronic timesheet system that will enable over 10,000 employees to enter daily work and leave activity over the internet. Cooperative efforts from the Departments/Offices of Finance, Technology Services, Management and Budget, and Human Resources resulted in a vendor selection and contract award to implement the project. Enhancements include significant staff productivity improvements and consistent application of the pay rules pursuant to the Personnel Regulations and bargaining unit agreements.

Enterprise Resource System: The Department of Technology Services is responsible for planning and budgeting for all initiatives related to the modernization of the County’s enterprise business systems. In early 2001, the County contracted with ASPEN Systems to conduct an Enterprise Resource Planning (ERP) implementation feasibility study. This resulted in the delivery of a Program of Requirements (POR). In 2004, MCPS and the County submitted a joint Technology Investment Fund (TIF) request, which was approved by the County Council, to undertake a more detailed requirements analysis in order to position the County for procurement of an ERP.

Health and Human Services

Medicaid Waiver: In FY04, the Department of Health and Human Services (DHHS) completed a three-year phase-in and fully implemented the Medicaid Waiver for Home and Community Based Services for Older Adults (Waiver). The Waiver serves people aged 50 and above who meet the criteria for a ‘nursing home’ level of care. Through participation in the Waiver, eligible clients remain in the community while receiving a variety of services including: personal care, home modifications, home delivered meals, personal emergency response systems, caregiver training (for their families), assisted living services and others. The local Area Agency on Aging administers the Waiver and provides the required medical assessments and case management. Private sector agencies provide these services and receive compensation directly from Medicaid. Currently, over 300 clients are receiving an estimated \$11 million in services.

Federal Financial Participation: DHHS successfully negotiated with the State Department of Health and Mental Hygiene to make a Federal Financial Participation (FFP) reimbursement claim to the federal government. No other jurisdiction in Maryland has been able to accomplish this, in part because the County invests vastly more money in mental health services than does any other jurisdiction in the state. Enhanced federal claiming enabled the County to prevent elimination of key positions when the State cut the local mental health administrative budget by more than \$900,000. While the County has not yet received final approval from the federal government on this new claim, DHHS anticipates that the claim will more than offset the State cuts.

Public Health Services: DHHS Public Health Services successfully achieved Public Health Ready Certification, accomplishing goals in key areas required to effectively respond to public health emergencies. The County was one

of 11 jurisdictions across the country to be awarded certification by the National Association of City and County Health Officials (NACCHO). Achievements required for certification include: preparedness planning; individual worker competence, and demonstration of readiness through drills and exercises. Over 500 public health staff received skills and competency training throughout the year and participated in drills and exercises, including an interagency exercise to test operational plans for mass vaccination.

Public Safety

Public Safety Communications System: The Departments of Fire and Rescue Service (DFRS) and Police transitioned from its two-way radio communications system to a new 800 MHz radio and mobile data communications system providing improved coverage, reliability and interoperability in late July 2003. The new public safety communications system included a new computer-aided dispatch system, automatic vehicle location and route recommendations, mobile data terminals and records management systems. In addition to fire and police, the communications systems include municipal police, Sheriff, highway operations, public health, and hospitals. Interoperable voice communications now exist among most jurisdictions and agencies in the region.

Integrated Justice Information System (IJIS): Through a \$3.1 million contract with BearingPoint Inc., the County is implementing an integrated criminal justice information system. The Integrated Justice Information System (IJIS) is a Web-based system that will enable the County to integrate disparate public safety systems. The system will enable the County's public safety and criminal justice agencies, including police, parole officers, courts, and public health organizations, to share information vital in making key decisions on a day-to-day basis.

Homeland Security and Emergency Preparedness: The County's Emergency Preparedness Initiative (EPI), established in FY02, continued to be a top priority in FY04 for the police, fire departments, and other county agencies. Plans and protocols for first responders, local government, businesses, and schools were developed for the Homeland Security's threat alert announcements. Exercises involving incidents related to bio-terrorism, dirty bombs and terrorists' attacks on infrastructure were conducted by the Emergency Management Group to improve the County's readiness, as well as the County's coordination with other federal, state and local agencies. Training was conducted with hospitals on decontamination by the DFRS HAZMAT team to improve medical readiness for bio-terrorist incidents. Several federal grants have enhanced the County Executive and County Council's initial General Fund investment. The Police Department deployed its new command bus, Field Com 1 (FC1) at a cost of \$1 million. This state-of-the-art response vehicle greatly enhances the ability to respond to emergencies and major incidents. The police department, acting as the lead agency, has procured and distributed approved Personal Protective Equipment (PPE) for all law enforcement entities operating within the county's borders. Utilizing Homeland Security Grant Funds (\$560,000- police allocation), additional PPE and other equipment has been secured for the newly formed SERT (Special Events Response Team). This multi-agency group operating out of the Special Operations Division is trained and equipped to respond to WMD, HAZMAT, and civil disturbance events.

Criminal Investigation and Suppression: The Department of Police formed and activated two critical units in FY04 to address the growing trends and community concerns relative to firearms and gang activities. The Firearms Investigation Unit began as a one-year temporary proactive unit and is now permanent. Objectives are to target individuals who illegally possess and/or sell firearms. In 2003, the 'task force' seized 374 firearms and made 96 arrests. The Police Department has assigned Gang Coordinators to each of the six police districts. The Gang Coordinators work in concert with dedicated officers from the Sheriff's Department and M-NCPPC Police Department to comprise the newly formed "Gang Task Force" pilot initiative.

Public Works and Transportation (Including Parking Lot Districts)

Three Parking Garages Opened: The Department of Public Works and Transportation (DPWT) opened a parking garage at the Grosvenor Metrorail Station. This garage will be operated by WMATA and provides 1,483 additional parking spaces for this heavily used Metro station. The Grosvenor garage cost approximately \$28.9 million. DPWT also opened two new garages in Silver Spring; the Wayne Avenue Garage and the Town Square Garage provide a total of approximately 3,080 spaces in conjunction with the opening of the fully redeveloped Silver Spring Town Center. The Silver Spring garages cost approximately \$67.7 million and feature the latest pay-on-foot technology.

Go Montgomery!: In July 2002, after an assessment of the County's transportation needs, the County Executive announced the Go Montgomery program. In FY04, the Council supported the program with \$20.1 million in appropriations. Major projects provided for by these appropriations include:

- Reliability and frequency improvements on bus routes;
- Design or construction of five roads;
- Addition or acceleration of fifteen facility planning studies of capacity generating projects;
- Final design of the expanded Brookeville Service park to support expansion of the Ride-On fleet; and
- Pedestrian safety enhancements.

Compressed Natural Gas (CNG) Fueling Station: DPWT completed construction on the state of the art CNG fueling station at a cost of \$3.8 million. The station converts standard pressure natural gas to CNG and provides fast-fill capability for a total of 79 CNG buses and can accommodate future expansion for additional CNG buses. Because of value engineering, construction costs have been reduced by \$700,000 or 18 percent, which makes the project the lowest cost per square cubic feet per minute of delivered gas in the nation. It is also the first site in the nation with all of its equipment built above ground, which significantly facilitates inspection, maintenance, and repair. The County's commitment to reducing greenhouse gas emissions and meeting EPA environmental standards is underscored by the purchase of 15 additional CNG buses in FY04, which will replace older diesel buses.

Liquor Control

Warehouse Update and Expansion: The design of a new 52,000 square foot climate controlled warehouse addition has been completed and construction will begin in FY05. In addition, the current warehouse space will be renovated to include air conditioning, which will bring the Department of Liquor Control (DLC) into compliance for product handling and will provide air conditioning to the last work area in the County. Total cost is estimated at \$7.3 million.

System Replacement: DLC signed a contract on June 11, 2004, with AMX International for redesign and replacement of the current retail, wholesale and financial computer systems with an ERP system. The new system promises the ability to expedite the inventory and routing processes, keep track of all products entering and leaving the warehouse in real time, implement the use of scanners as part of the inventory and delivery processes, and incorporate a new point-of-sale system and a new comprehensive financial management system. Total cost for replacement, including hardware, software, data conversion, training and consulting services, is estimated at \$7 million.

AWARDS AND ACKNOWLEDGMENTS

Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to Montgomery County, Maryland, for its CAFR for the fiscal year-ended June 30, 2003. Montgomery County has received the Certificate of Achievement more times than any other county in the nation – thirty-four times – as early as 1951 and consecutively for thirty-two years, since 1972.

The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of state and local government financial reports. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized CAFR. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. The Department of Finance believes its current report continues to meet the Certificate of Achievement Program's requirements and is submitting it to GFOA to determine its eligibility for another certificate.

Distinguished Budget Presentation

GFOA presented an award of Distinguished Presentation to Montgomery County, Maryland, for its annual budget for the fiscal year beginning July 1, 2003. In order to receive this award, a governmental unit must publish a document that meets program criteria as a policy document, as an operations guide, as a financial plan, and as a communications device. The award is valid for a period of one year only. Montgomery County has received this award consecutively since 1984, the year the program was established. The Office of Management and Budget believes the current budget continues to conform to program requirements and is submitting it to GFOA to determine its eligibility for another award.

Other Financial Management Awards

The County has recently received several other awards for its strong financial management. The Finance Electronic Transfer Tax Application, which reengineered the simple deeds and deeds of trust business processes, received a 2003 Achievement Award from the National Association of Counties (NACO); the application was also named a 2003 Top 25 Technology Solution by Public Technology, Inc. (PTI). The Finance government-to-business (GTB) Tax Lien Sale Process, which involves a streamlined, simplified sealed bid group process, coupled with random groupings of tax liens and a high bid premium, received a 2004 Achievement Award from NACO. During the year, the County was also named the Best Overall Community in North America by Cayenta, Inc., a software management company. The award was based on the County's strong financial management and strategic planning, growing economy, and well-designed capital and infrastructure management.

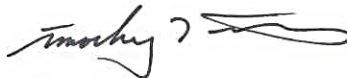
Acknowledgments

The preparation of this report on a timely basis could not be accomplished without the efficient and dedicated services of the staff of the County's Department of Finance. I express my appreciation to all participants who assisted and contributed to its preparation. I particularly express my sincerest appreciation to Karen Q. Hawkins, CPA, Controller, and her staff, particularly the General Accounting, Grants Accounting, and Administration Sections, for their outstanding performance in the preparation of this report. A list of individuals whose dedicated efforts produced this report is provided separately after this letter. A special appreciation is extended to the finance and accounting managers of the component units whose cooperation greatly facilitated the preparation of this report. I express my appreciation to the County Executive, the members of the County Council and the Chief Administrative Officer and their staffs for their continuing interest and support in planning and conducting the financial operations of the County in a responsible and progressive manner.

USE OF THIS REPORT

This report, and other financial information prepared by the Montgomery County Department of Finance, can be accessed on the County's website at <http://www.montgomerycountymd.gov> (see Services (A-Z), Finance, Financial Reports). Copies of this report are also being placed in the County Library System for use by the general public.

Respectfully submitted,



Timothy L. Firestine
Director of Finance

ACKNOWLEDGMENTS

The following individuals' efforts were instrumental in closing the County's funds, and in preparing this Comprehensive Annual Financial Report:

Department of Finance

Wayne Johnson	Stephen M. O'Malley
Joyce E. Boyd	Catherine Patterson
Marilyn Clement	Nora A. Ravarra
Michelle S. Hwang	Danielle R. Snowden
Jay Narang	Claudia L. Stalker
Christine V. Ullmann	Darane Tiev
Michael E. Edelin, Sr.	Jan Clagett
Nancy C. Foster	Josephine Gilbert
Sara Ghoshal	Michael Lawton
Timothy D. Hughes	Dolores Horne
Karen J. Jackson	Denise E. Siegel
Susan E. Kaplan	Wayne Hsin
Felix O. A. Ogunba	

Department of Liquor Control

Andy Brown Richard J. Duthoy

Department of Public Works and Transportation

Richard D. Hands Jo Ann Byrum
Florence Bartlett-Vanderpuye

The following individuals provided data and information for inclusion in this report:

County Government

Department of Finance

Jennifer Barrett	Nancy Moseley
Michael Coveyou	David Platt
Terry Fleming	Marty Utermohle
Ray Gulhar	Glenn Wyman
Robert Hagedoorn	John Swaney

Department of Public Works and Transportation

Rick Siebert Bill Davidson
Edna McGraw Tom Kusterer
Luz Rodriguez
Richard Taylor and the Print Shop

Office of Management and Budget

Beverley Swaim-Staley	Sunil Pandya
Beryl Feinberg	Heidi Metzger

Office of Public Information

Thomas Whorton

Component Units

Montgomery County Public Schools

Larry A. Bowers	Susanne G. DeGraba
Robert J. Doody	Jack Dodson

Housing Opportunities Commission

Cornelia Kent Eugenia Pascual

Montgomery Community College

Marshall Moore	Linda Hickey
Kenneth Mullinix	

Montgomery County Revenue Authority

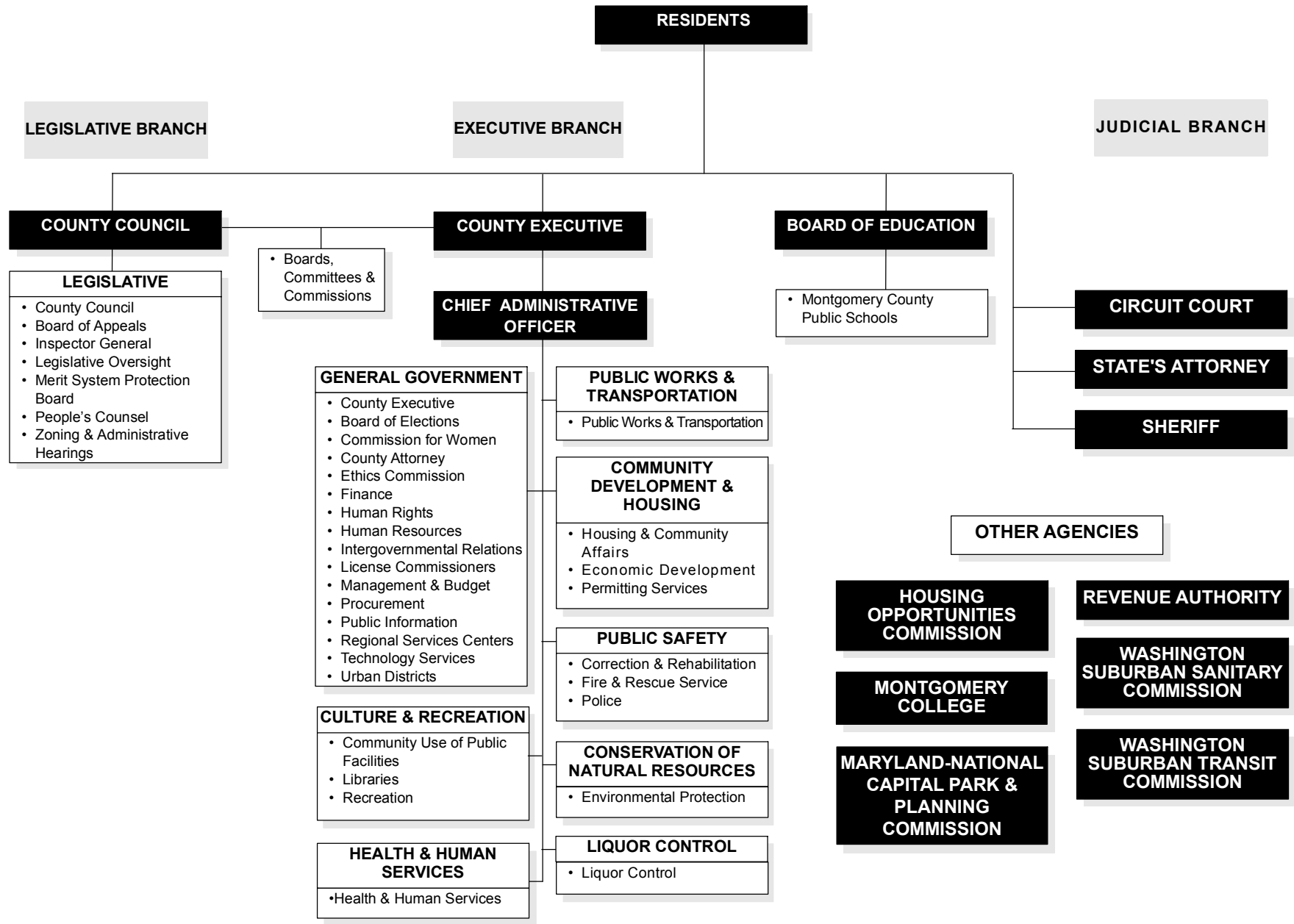
Linda Decker

Bethesda Urban Partnership, Inc.

Deborah Williams

Appreciation is extended to all those in the County Government who take a leadership role in the year-end closing processes and the audit process, including staff in the Department of Finance (Accounts Payable, Information Technology, Payroll, and Internal Audit), Office of Management and Budget, Office of Procurement, Department of Technology Services, and Board of Investment Trustees. Appreciation is also extended to employees in all County departments and agencies who participate in the year-end processes.

MONTGOMERY COUNTY, MARYLAND FUNCTIONAL ORGANIZATION CHART



MONTGOMERY COUNTY, MARYLAND
ELECTED OFFICIALS
June 30, 2004

COUNTY EXECUTIVE
Douglas M. Duncan

COUNTY COUNCIL

Steven Silverman
Tom Perez

President
Vice President

Phil Andrews
Howard Denis
Nancy Floreen
Michael Knapp

George Leventhal
Marilyn Praisner
Michael L. Subin

Other Elected Officials

Administrative Judge Circuit Court
Clerk of the Circuit Court
Register of Wills
Sheriff
State's Attorney

Ann S. Harrington
Molly Q. Ruhl
Joseph M. Griffin
Raymond M. Kight
Douglas F. Gansler

APPOINTED OFFICIALS

Chief Administrative Officer

Board of Appeals

Correction and Rehabilitation

County Attorney

County Council

Economic Development

Environmental Protection

Finance

Fire and Rescue Service

Health and Human Services

Housing and Community Affairs

Human Resources

Inspector General

Intergovernmental Relations

Legislative Oversight

Liquor Control

Management and Budget

Merit System Protection Board

People's Counsel

Permitting Services

Police

Procurement

Public Information

Public Libraries

Public Works and Transportation

Recreation

Technology Services

Zoning and Administrative Hearings

Bruce Romer

Katherine Freeman

Arthur M. Wallenstein

Charles W. Thompson, Jr.

Stephen B. Farber

David W. Edgerley

James A. Caldwell

Timothy L. Firestine

Gordon A. Aoyagi

Carolyn W. Colvin

Elizabeth B. Davison

Joseph Adler

David A. Newcomer

Melanie L. Wenger

Karen Orlansky

George Griffin

Beverley Swaim-Staley

Waddell Longus

Martin Klauber

Robert Hubbard

J. Thomas Manger

Beatrice P. Tignor

David S. Weaver

Harriet Henderson

Michael C. Hoyt

Gregory A. Baylor

Alisoun K. Moore

Francoise Carrier

Montgomery County Officials, Concluded

COMPONENT UNIT OFFICIALS

Montgomery County Public Schools

Board of Education:

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Patricia B. O'Neill, Vice-President

Kermit V. Burnett

Gabriel Romero

Charles Haughey

Sagar Sanghvi,

Walter N. Lange

Student Member

Henry Lee

Jerry D. Weast, Superintendent of Schools

Montgomery County Revenue Authority

Board of Directors:

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Carol McGarry, Secretary-Treasurer

Peter L. Gray

John Lane

Herbert L. Tyson

Scott Reilly, Ex-Officio

Marc D. Atz, Executive Director

Bethesda Urban Partnership, Inc.

Board of Directors:

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Jack D. Hayes, Vice Chair

Michele Horwitz Cornwell, Treasurer

Patricia A. Harris, Secretary

Robert E. Hebda

Jason Hoffman

Renee Kotz

Page Lansdale

Dee Carl Metz

Elliot Schnitzer

Deborah Snead

W. David Dabney, Executive Director

Montgomery Community College

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Ryan McGoff, Student

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Charlene R. Nunley, President and Secretary-Treasurer

Housing Opportunities Commission of Montgomery County

Commissioners:

Richard Y. Nelson, Jr., Chair

Norman Cohen, Vice Chair

Y. Monroe Galloway, Chair, Pro Tem

Roberto R. Pinero

Ralph D. Bennett, Jr.

Lakeyia L. Thompson

Michael J. Kator

D. Scott Minton, Executive Director and Secretary Treasurer

INDEPENDENT AUDITORS

KPMG LLP
2001 M Street, N.W.
Washington, DC 20036

Elected Officials

Montgomery County, Maryland



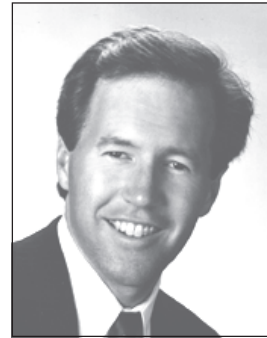
Douglas M. Duncan
County Executive



Steven Silverman
Council President



Tom Perez
Council Vice-President



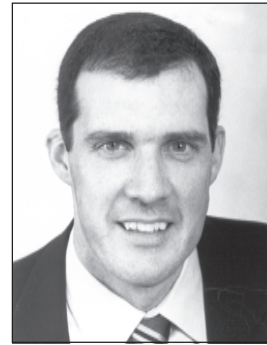
Phil Andrews
Council Member



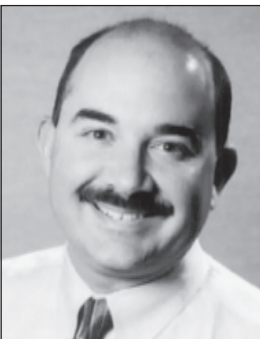
Howard Denis
Council Member



Nancy Floreen
Council Member



Michael Knapp
Council Member



George Leventhal
Council Member



Marilyn Praisner
Council Member



Michael L. Subin
Council Member